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IN THE

Supreme Court of the United States

OCTOBER TERM, 1969

No. .....

MANUFACTURERS HANOVER TRUST COMPANY, as Trustee of the First and Refunding Mortgage of THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY,

Appellant,

v.

UNITED STATES OF AMERICA and INTERSTATE COMMERCE COMMISSION, *et al.*,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

JURISDICTIONAL STATEMENT

Appellant appeals from a final Decree of the United States District Court for the Southern District of New York dated and entered on September 11, 1969, and submits this Jurisdictional Statement to show that this Court has jurisdiction of this appeal and that a substantial question is presented.

The Opinions Below*

The Opinion of the Three Judge Court of the Southern District of New York (the "Three Judge Court") dated

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* The opinions below are separately bound in an Appendix entitled "The New Haven Railroad: Terms of Sale and Inclusion

June 18, 1969 (pp. 400-443a) pursuant to which the above final decree was entered has not yet been reported. The Fourth Supplemental Report and Order of the Interstate Commerce Commission (the "Commission") (pp. 112-220a) and the Fifth Supplemental Report of the Commission, as revised (pp. 222-28a), to which the decree relates, are reported at 334 I.C.C. 25 and 334 I.C.C. 528, respectively.*

The opinion and order of the Three Judge Court dated July 10, 1968 (pp. 323-83a), which relates to matters which are the subject of this appeal, is reported at 289 F. Supp. 418. The Commission's Second Supplemental Report and Order (pp. 1-111a) to which that opinion and order relate, is reported at 331 I.C.C. 643.**

Jurisdiction

This Court has jurisdiction of this appeal under 28 U.S.C. § 1253. The final decree of the Three Judge Court was filed on September 11, 1969. This appeal was filed on October 9, 1969.

At or about the time of the filing of this statement, Appellant and others are filing with this Court, pursuant to

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Cases" which is being filed herewith. References to that Appendix are identified by the letter "a" following the page reference. References preceded by "NHI" or "R" are to exhibits at the hearings before the Commission's Examiners and references preceded by "Tr." are to pages in the hearing transcript.

* The opinion of the Reorganization Court (the United States District Court for the District of Connecticut), dated May 28, 1969 (pp. 277-306a), which deals with the same issues (viz., valuation of the assets sold and the consideration to be paid), as the opinion of the Three Judge Court dated June 18, 1969, has not yet been reported.

** The Opinion of the Reorganization Court, dated August 10, 1968 (pp. 237-60a), which deals with the same issues as the Three Judge Court opinion dated July 10, 1968, is reported at 289 F. Supp. 451.

28 U.S.C. § 1254(1) and this Court's Rule 20, Petitions for Certiorari to the United States Court of Appeals for the Second Circuit, before judgment in that Court, to review so much of the Judgment of the United States District Court for the District of Connecticut (the "Reorganization Court"), as decided essentially the same issues (the so-called "Step I" issues) which are involved in this appeal.

Questions Presented

1. Whether an insolvent railroad which has been required to continue in operation for over seven years at substantial loss and consequent erosion of the security of its bondholders, may be required under the United States Constitution and Section 5 of the Interstate Commerce Act, to accept consideration worth substantially less than the fair liquidation value of the assets being sold, including specifically the following questions:

(a) Whether it is constitutionally permissible or in accordance with the requirements of Section 5 of the Interstate Commerce Act for the Commission to reduce the net liquidation value of the New Haven assets being sold by an allowance for the assumed consequences of a hypothetical delay in the commencement of liquidation caused by the fact that the Commission and the courts might postpone abandonment for a further period of one year beyond the valuation date selected by the Commission, where the railroad has been operating at a loss in reorganization, at the expense of its bondholders, for more than seven years;

(b) Whether it is constitutionally permissible or in accordance with the requirements of Section 5 of the Interstate Commerce Act for the Commission to make a further reduction in what it has found to be the net liquidation value of the railroad in order to give Penn Central the equivalent of an entrepreneur's profit or compensation for

an entrepreneur's assumed risk on the theory that the assets of the New Haven are to be sold "in bulk";

(c) Whether it is constitutionally permissible or in accordance with the requirements of Section 5 of the Interstate Commerce Act for the Commission to treat as valueless, in determining the liquidation value of the railroad, important assets and elements of value including the following:

(1) the right of the railroad to fully-paid access to Grand Central Terminal and its correlated right to the income formerly used to defray Terminal expenses;

(2) the going concern value of the railroad as a utility in being which is to be continued in operation where this is an element of value under the condemnation law of a state or states where a part of the railroad's assets are located;

(d) Whether it is constitutionally permissible or in accordance with the requirements of Section 5 of the Interstate Commerce Act for the Commission, in spite of evidence from both sides that its calculations are erroneous, to refuse on remand to consider and determine the proper amount of the discount necessary to determine the present value of the net receipts of liquidation which are assumed to be received over a period of time;

(e) Whether it is constitutionally permissible or in accordance with the requirements of Section 5 of the Interstate Commerce Act for the Commission to find on the basis of matters dehors the record that one appraisal of certain real estate owned by the New Haven, namely the Harlem River and Oak Point Yards, is correct and a second appraisal is incorrect, and whether the valuation of this property is supported by substantial evidence;

(f) Whether it is constitutionally permissible or in accordance with Section 5 of the Interstate Commerce Act for the Commission to achieve a purported equality between what it has found to be the adjusted liquidation value of the assets conveyed by the New Haven and the value of the consideration to be received by the New Haven by assigning grossly inflated values to the consideration furnished by Penn Central, including shares of its common stock, and whether the modifications made by the Three Judge Court are adequate to cure this deficiency.

2. Whether, in view of the terms and conditions of the orders of this Court and of the Commission approving the merger of Penn and Central, the Commission, under the Constitution and Section 5 of the Interstate Commerce Act, may properly require the bondholders of the New Haven to absorb the New Haven's operating losses during the eleven-month period between the Penn Central merger and the inclusion of the New Haven in the merged railroad.

Constitutional Provisions and Statutes Involved

The following provisions of the United States Constitution and of the United States Statutes, which are believed to be involved in the determination of this case, are set forth in the Appendix entitled "The New Haven Railroad Terms of Sale and Inclusion Cases" which is being filed herewith, beginning at page 453a:

(1) The Fifth Amendment to the United States Constitution;

(2) Sections 1(18), 1(20) and 5(2) of the Interstate Commerce Act, 49 U.S.C. §§ 1(18), 1(20) and 5(2); and

(3) Sections 77(b) and 77(e) of the Bankruptcy Act, 11 U.S.C. §§ 205(b) and 205(e).

Statement

On February 1, 1968, The Pennsylvania Railroad Company ("Penn") and The New York Central Railroad Company ("Central") were permitted to merge on terms and conditions which had been established by the Commission (327 I.C.C. 475, 328 I.C.C. 304) and approved by this Court (389 U.S. 486) over the objections of certain of the New Haven bondholders. Among the conditions of the Penn Central merger was the following:

> "8. The Pennsylvania New York Central Transportation Company shall be required to include in the transaction all the New York, New Haven and Hartford Railroad Company—the inclusion of passenger operations being subject to the findings and determinations of the Commission as set forth in Finance Docket No. 23831 issued simultaneously with this report—upon such fair and equitable terms as the parties may agree subject to the approval of the Bankruptcy Court and the Commission. Within 6 months after the date this report is served, the parties shall file with the Commission for its approval, a plan for such inclusion. In the event the parties are unable to reach an agreement (and subject to approval by the Bankruptcy Court) such inclusion shall be upon such fair and equitable terms and conditions as the Commission may impose.
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> Jurisdiction is hereby reserved for such purposes. Consummation of the merger by applicants shall indicate their full and complete assent to these requirements."* (327 I.C.C. at 553)

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* By report and order dated April 6, 1966, and published simultaneously with its initial report approving the merger, the Commission denied the New Haven Trustees' application for permission to discontinue long-haul passenger trains (327 I.C.C. 151) which had been filed in March, 1965.

Reorganization Court approval was required because the New Haven had been in reorganization, under Section 77 of the Bankruptcy Act, since July, 1961. (In fact, it had had no net income since 1956 and incurred continuing substantial deficits in both net railway operating income and net income before and during reorganization (cf. pp. 283-86a).*)

Before this Court approved the Penn Central merger, the Commission had issued its Second Supplemental Report (331 I.C.C. 643, p. 1a), in which it apparently found, using an assumed liquidation date of December 31, 1966, that the net liquidation value of the operating assets of the New Haven was $128.9 million, which it "rounded off" to $125 million, and the fair value of the consideration to be paid by Penn Central specified in an agreement (the "Purchase Agreement"), among Penn, Central and the New Haven's Reorganization Trustees** was $123.6 million, which it like-

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* The New Haven Trustees had concluded during their first six months of Trusteeship that the New Haven would have to be liquidated unless it could be merged with a trunk line carrier. In 1962, they intervened in the Penn Central merger case in order to seek to be included in that merger and negotiations on the terms of the inclusion commenced among Penn, Central and the New Haven Trustees, in June, 1964.

An application made in April, 1967 by the Bondholders' Committee to terminate the reorganization for the purpose of commencing liquidation was denied by the Reorganization Court in a decision dated February 13, 1968 (281 F. Supp. 65).

** The Purchase Agreement had not been submitted to the Reorganization Court for its approval and had been negotiated and executed without any notice to or participation by the New Haven's bondholders or their representatives. Negotiations between the New Haven Trustees and Penn and Central on the terms of the New Haven's inclusion had been going forward since June, 1964 and basic agreement for the sale of the New Haven's assets to Penn Central and the price to be paid had been reached in November, 1964, although the terms of the Agreement were not made public until March 31, 1965, two days after the publication of the Hearing Examiner's Report on the Penn Central merger.

wise "rounded off" to $125 million.* In view of this purported equality between the liquidation value of the New Haven assets and the value of the consideration to be paid, the Commission approved the terms of the Agreement, with one modification,** as the so-called "Step I" of the Plan of Reorganization of the New Haven and as satisfying the obligation of Penn Central upon their merger under Section 5(2) of the Interstate Commerce Act and under Condition 8, quoted above, of its order approving the Penn Central merger.

In the spring of 1968, parallel proceedings to review the Commission's Second Supplemental Report were commenced—(i) proceedings under Section 77 of the Bankruptcy Act before the Reorganization Court on the Commission's certification of the modified Purchase Agreement as "Step I" of the Plan of Reorganization of the New Haven; and (ii) a consolidated proceeding brought pursuant to 28 U.S.C. § 1336, 1398, 2284, 2321-25, by Petitioner and other bondholder interests before the Three Judge Court to review the Commission's order insofar as it related to the Interstate Commerce Act.

The Three Judge Court, in an opinion and order filed May 6, 1968 (289 F. Supp. 418, pp. 323-83a), disapproved

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* The consideration took the form substantially of (a) 950,000 shares of Penn Central common stock, (b) $23,000,000 principal amount of Penn Central 5% bonds, (c) $8,000,000 cash, (d) assumption by Penn Central of certain obligations of the New Haven, principally under a mortgage of the Boston & Providence, and (e) $9.5 million in so-called "Purchase price adjustments," which reduced the New Haven's obligations to Penn Central under the Purchase Agreement.

** Responding to an application by the bondholders that Penn Central should be required to take over New Haven operations by lease or otherwise immediately upon the merger, the Commission added to the Agreement a provision requiring Penn Central to assume a portion of the operating losses of the New Haven for the period between the Penn Central merger and inclusion of the New Haven, computed on a sliding scale formula.

the Commission's order on the ground that the price Penn Central was required to pay appeared too low by $45-50 million (289 F. Supp. at 440, p. 358a).* The Reorganization Court filed an opinion and order on August 13, 1968 (289 F. Supp. 451, pp. 237-60a), in which it also disapproved the Plan on the ground that the consideration which Penn Central was required to pay was inadequate and stated that the additional consideration to be paid by Penn Central "might properly fall within a range of $33,000,000 to $55,000,000." (289 F. Supp. at 465, p. 256a). Both courts remanded the case to the Commission.

After an abbreviated hearing, the Commission issued its Fourth Supplemental Report and Order, dated November 25, 1968 (334 I.C.C. 25, pp. 112-221a). The Commission found that the New Haven assets to be sold to Penn Central had a net liquidation value of $162.7 million, $33.8 million more than it had found in its Second Supplemental Report, but then introduced as "Other Pricing Considerations" (334 I.C.C. at 53-63, pp. 140-50a), two entirely new concepts, an abandonment delay discount and a bulk sales discount which "adjusted" the net liquidation value of the New Haven assets downward by $22.1 million, from $162.7 million, to $140.6 million.**

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* The Three Judge Court also disapproved the Commission's "loss-sharing" formula because of its "in terrorem" aspects (289 F. Supp. at 444, pp. 366-67a). The Reorganization Court seemingly agreed (289 F. Supp. at 464-65, p. 255a).

** Ironically, Commission counsel had admitted in the Three Judge Court hearing that in its original decision the Commission had made a double deduction of approximately $14.6 million (289 F. Supp. at 450, pp. 380-81a). By simply correcting this error and adding it to the net liquidation value found in the Commission's Second Supplemental Report, one would get a larger liquidation value—$143.5 million—than the Commission arrived at in its second effort, without any concern for new "pricing considerations" and wholly disregarding the other valuation errors noted by the courts.

Of the $22.1 million reduction, $15.4 million was deducted because of the assumed effect of a one-year delay in liquidation beyond the valuation date (December 31, 1966) which the Commission had selected on the theory that it would take that long to obtain approval to abandon the railroad. An additional $6.7 million was deducted on the assumption that liquidation would necessarily occur on a bulk rather than a piecemeal basis, and the theory that an entrepreneur who purchased the land in bulk for resale would be entitled to additional compensation beyond that taken into account by the appraisal witnesses.*

Although the Commission received evidence on the value of Penn Central stock, which represented $83.1 million of the assumed value of the consideration to be paid by Penn Central, it adhered to its original determination that the "intrinsic" value of the stock is $87.50 per share, even though the stock had a market value of $52⅜ per share on December 31, 1966, the valuation date used by the Commission for the New Haven assets, and a market value of around $60-65 per share during November, 1968 when the Commission was deliberating. (The stock closed at 63⅜ on

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* The witness who proffered this theory had never seen any of the appraisals or read any of the appraisers' testimony (Tr. 29823-34, 29855, 29858-60, 29878). The basic valuation studies were put into evidence through the following witnesses: for the New Haven Trustees, by William Gordon, of Coverdale & Colpitts, Consulting Engineers; Frank A. Mason, Vice President of Meredith & Grew, Inc., appraisers; and Bradford Thompson, who headed the New Haven real estate department; for Penn Central, by Francis Gasparini, Central's General Real Estate Manager; Norman Hull, Central's assistant comptroller; and John R. White, Executive Vice President of James D. Landauer Associates, Inc., real estate consultants; and for the bondholders, by Paul O'Keefe, a real estate appraiser.

the actual closing date, December 31, 1968; since then, it has fallen steadily lower.)*

Parallel proceedings were again commenced—in the Three Judge Court** and in the Reorganization Court—to review the Commission's Fourth Supplemental Report. On this review, the result was a significant difference between the decision of the Reorganization Court and the majority opinion of the Three Judge Court, which has created the problem that this Court is now urged to resolve.

In its Opinion dated May 28, 1969, the Reorganization Court held that the "administrative delay" discount of $15,386,000 and the "bulk sale" discount of $6,695,000 should not be deducted from the amount of $162.7 million which the Commission had found to be the net liquidation value of the New Haven assets (pp. 281-94a). Both discounts, the Reorganization Court held, "illegally contravened the statute [Section 77]" (p. 281a). The Reorganization Court characterized the Commission's administrative delay discount as an "arbitrary device which the Commission hauled in by the heels" to reduce the liquidation value of $162.7 million which it found "because it felt that figure was too high to be fair and equitable to Penn Central" (p. 292a). The Three Judge Court (Weinfeld, J. dissenting) upheld the Commission in deducting the two discounts described above (pp. 411-18a).

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* As directed by the courts, the Commission eliminated the "in terrorem" provisions of its original loss-sharing formula, and simply required Penn Central to pay a lump sum of $5 million as its share of the New Haven's operating losses for the last eleven months of 1968, the period between the Penn Central merger and the New Haven's inclusion. This amount has been variously estimated at between 40% and 60% of the New Haven's actual loss for that period. Cf. 334 I.C.C. at 67, 73-74, pp. 154a, 160-61a, and discussion at pp. 39-41 *infra*.

** Pursuant to 28 U.S.C. §§ 1336, 1398, 2284, 2321-25.

The two courts also reached conflicting results on several other substantial points, including the following:

Items which Reduce Liquidation Value	Reorganization Court	A Majority of the Three Judge Court*
"Administrative Delay" Discount—$15,386,000	Rejected (pp. 279-92a)	Approved (pp. 411-16a)
"Bulk Sale" Discount—$6,695,000	Rejected (pp. 292-94a)	Approved (pp. 416-18a)
Items which Increase Liquidation Value		
Adjustments in the discount to present worth of net liquidation receipts	Approved an increase of $2,415,889 (p. 318a)	Tentatively approved an increase of $410,000 pending review by this Court (pp. 444-45a)
Adjustments in the valuation of the Harlem River and Oak Point Yards—$4,439,000	Approved (pp. 295-97a)	Rejected (p. 423a)

As a result of these disagreements, the two courts differ in their views as to the amount to which the New Haven is entitled by approximately $28 million.

Both courts rejected the bondholders' contentions that the valuation of the New Haven assets should be increased to take into account a number of items, including: (a) New Haven's right to fully-paid access to Grand Central Terminal and its correlated right to the income formerly used to

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* Judge Weinfeld agreed with the Reorganization Court, and disagreed with the majority of the Three Judge Court, with respect to the "administrative delay" (pp. 435-38a) and "bulk sale" discounts (pp. 438-39a) and the valuation of the Oak Point and Harlem River Yards; he apparently expressed no view on the question of the discount of net receipts to prevent value. He also disagreed with all the other judges as to the treatment of "loss-sharing" (Judge Weinfeld was of the view that Penn Central should bear all interim losses) (pp. 441-42a) and did not agree that the "underwriting" formula was a satisfactory solution to the Commission's overvaluation of the Penn Central stock (p. 442a).

defray its share of the expense of Terminal operations; (b) the "going concern" value of the New Haven; (c) the value of certain New Haven assets, notably its investments in other companies; and (d) the reduction of net liquidation value by $3 million for purported 1966 "depreciation".*

Both courts also agreed that the Commission erred in valuing Penn Central stock at $87.50 per share. The Reorganization Court developed *sua sponte*, and the Three Judge Court later adopted in substance, an "underwriting" formula under which, in essence, Penn Central must pay the difference between the market value of the stock nine years hence and $87.50, unless the market price of the stock previously reaches that figure (pp. 299-301a, 318-19a, 429-30a, 449-50a).**

The Questions Presented Are Substantial

In the context of this case, the existence of parallel proceedings in two courts of essentially coordinate jurisdiction affords perhaps the most convincing proof that the issues presented for review are in fact substantial ones.

Of the eight specific points upon which review is sought and which are discussed in detail below, the reviewing courts have reached diametrically opposite results with respect to four matters, totalling $28 million—(i) the dis-

* Two of these points, "going concern" value and the value of investments (by implication), were passed upon in the first decision of the Three Judge Court (289 F. Supp. at 435, pp. 347-49a), in its review of the Commission's Second Supplemental Report and Order. These issues were preserved by the Petitions seeking review of the Commission's Fourth Supplemental Report and Order and are properly before this Court on review of the Three Judge Court's final decree. *United States* v. *U.S. Smelting Co.*, 339 U.S. 189, 198-99 (1950).

** As noted previously, Judge Weinfeld dissented on this point (pp. 441-42a).

count for "abandonment delay"; (ii) the "bulk sale" discount; (iii) the appropriate amount of the adjustment in the discounted present value of future liquidation receipts; and (iv) the valuation of the New Haven's Oak Point and Harlem River Yards.

One member of the Three Judge Court, Judge Weinfeld, in addition to agreeing with the Reorganization Court's decision with respect to the "bulk sale" and "administrative delay" discounts and the valuation of the Harlem River and Oak Point Yards, has concurred with the position of Appellant on two additional issues, namely, (i) the proposition that Penn Central should be required to bear all of the New Haven's interim operating losses, and (ii) the proposition that the Bondholders may not be obliged to accept overvalued stock of Penn Central.* Finally, the Reorganization Court has indicated that it has reservations about the correctness of its treatment of a seventh issue, namely, the value of the New Haven's right of fully-paid access to Grand Central Terminal (pp. 314-15a).

There is no difference of opinion between the reviewing courts on the final question presented—namely, so-called "going concern" value—but it raises, we submit, an important question of the relevance of state-created principles of valuation in regard to the valuation criteria to be employed under the Bankruptcy Act and the Interstate Commerce Act.

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* While the decision appealed from adopts in substance the "underwriting" formula for Penn Central stock which the Reorganization Court developed, this formula is one which was never proposed in any form by any party and raises a number of serious questions (discussed at pp. 29-31 *infra*) which, we respectfully submit, could not have been fully considered by either of the reviewing courts.

1. ***The majority opinion of the Three Judge Court accepts a construction of the term "fair liquidation value" which results in a standard which is neither constitutional nor in conformity with the requirements of Section 5 of the Interstate Commerce Act (nor Section 77 of the Bankruptcy Act).***

The Three Judge Court has affirmed the Commission's decision that the term "liquidation value" as a standard of value under Section 5 of the Interstate Commerce Act, Section 77 of the Bankruptcy Act and the "Due Process" Clause of the United States Constitution contemplates reductions in the liquidation value it finds to take into account its own administrative delays and entrepreneurial profit for the purchaser.

As Judge Weinfeld noted in his dissent, both the Reorganization Court and the Three Judge Court were in purported agreement that the constitutional and statutory standard to be applied in this case is whether the New Haven has received in consideration the fair value of what it has sold, which, at least in this case, is the fair liquidation value (p. 434a).*

The difficulty here is that, on remand, the Commission, while disclaiming any obligation to award liquidation value, has introduced two totally novel concepts—in the way of "adjustments" to net liquidation value—which have the effect of awarding at least $22.1 million less than liquidation value, and has explained those reductions as having been made in the public interest and in the interest of fairness to Penn Central (334 I.C.C. at 54-56, pp. 141-43a). Although it originally held that "liquidation value" represents the minimum price which must be awarded to the

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* Any other test, we submit, would be contrary to the decisions of this Court in *Brooks Scanlon Co. v. Railroad Commission*, 251 U.S. 396 (1920); *Bullock v. Railroad Commission*, 254 U.S. 513 (1921); and *Railroad Commission v. Eastern Texas Railroad*, 264 U.S. 79 (1912).

New Haven in this case—and the members of that Court apparently still adhere to that view—the majority of the Three Judge Court has nevertheless taken the view that it can affirm such a procedure without reaching the statutory or constitutional question (pp. 407-11a). Such an approach, we submit, is defensible only if the phrase "liquidation value", whatever its nominal significance as a standard of fairness and equity and of constitutionality, is deemed to be no more than a symbolic label without substantive content.

The fact is that, on the Commission's own analysis, the New Haven has been awarded far less than its fair liquidation value, and the unavoidable question is whether such a procedure is permissible under the statutes or the Constitution.

Acting under Section 77 of the Bankruptcy Act, the Reorganization Court has flatly held that the standard of fairness required by the statute and the constitution is fair liquidation value, and has accordingly disallowed the adjustments. Judge Weinfeld has reached substantially the same result.

The question is an important one and may be one of more or less first impression (although we will argue that it is answered by this Court's decision in *Brooks-Scanlon* and its sequels) because, so far as we are aware, the Commission has consistently recognized that in cases where a railroad is to be abandoned and sold, the Commission's power to require sale to a purchaser who will continue railroad operations is conditioned upon the seller receiving a price at least equal to "scrap value."*

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* See e.g., *Tennessee Central Ry. Co. Abandonment*, 331 I.C.C. 433, 454-5 (1968); *New York Central R. R. Co. Acquisition of Chicago, Attica & Southern R.R.*, 187 I.C.C. 527 (1932); *New York Central R.R. Co. Acquisition of Boyne City, G&A. R.R.*, 180 I.C.C. 538, 564-5 (1932); *Jay Street Connecting R.R. Abandonment*, 307 I.C.C. 137, 163 (1959).

This historical position of the Commission is, we submit, one which the Constitution and the Interstate Commerce Act (as well as the Bankruptcy Act) require. *Railroad Commission* v. *Eastern Texas Railroad*, 264 U.S. 79, 85 (1924). Its effort to abandon that position in this case raises a substantial and important question of constitutional law.

Further, the majority opinion in the Three Judge Court rests affirmance of the Commission in respect of the "administrative delay" and "bulk sale" discounts on a process of reasoning which is clearly far different from that of the Commission and which assumes findings of fact by the Commission which the Commission did not make and, on the basis of the evidence, could not have made.

A. The Commission and the Three Judge Court erred in reducing liquidation value by $15.4 million for alleged delay in commencing the abandonment.

In its Second Supplemental Report dated November 16, 1967, the Commission adopted as its valuation date December 31, 1966, and generally accepted appraisals of the property made as of December 31, 1965 (331 I.C.C. at 659-60, 688, pp. 17-18a, 46a.* The choice was an arbitrary one;

* The New Haven Trustees' liquidation value studies, which the Commission generally accepted, were prepared in the fall of 1966, and used December 31, 1965 as a valuation date. Penn Central's liquidation value evidence, which the Commission generally rejected, was prepared in the early part of 1967 and used December 31, 1966 as the valuation date, except as to land, which was appraised as of December 31, 1965. No one has ever contended that either December 31, 1965 or December 31, 1966 has any special significance or is more than an arbitrarily chosen convenience. The memorandum of understanding which formed the basis of the Purchase Agreement, reflects a basic understanding reached in November, 1964 (from which the bondholders were excluded). The Agreement was dated April 21, 1966; the sale was consummated on December 31, 1968.

at that time no one knew with any precision when inclusion would take place.

As one part of its valuation decision, the Commission accepted, in its Second Supplemental Report, a six-year liquidation period as the time during which the railroad assets could be dismantled and sold. The courts sustained that judgment and the Commission has adhered to it.

In its original decision, the Three Judge Court rejected Penn Central's argument that there would be a delay in liquidation because abandonment proceedings might be necessary, saying:

> ". . . a considerable portion of the losses [of the New Haven after December 31, 1961] will be borne by the New Haven estate, and there would be no justification for a double deduction. Beyond that, the Commission had to pick a date for valuation and December 31, 1966 was a reasonable choice. If we were to posit a liquidation beginning only some years hence, we could not simply deduct interim cash losses and depreciation, but would have to ask the Commission to revalue the estate. . . ." (289 F. Supp. at 438-39; p. 355a)

On remand, however, the Commission nevertheless revived the theory, but adopted a new measure of its consequences, namely, that the net liquidation value it found (of $162.7 million) had to be further reduced by three factors:

(1) increase in the discount to present worth for a one year delay	$ 7,946,000
(2) one year's preservation costs	4,940,000
(3) one year's accrual of real estate taxes	2,500,000
	$15,386,000

A majority of the Three Judge Court accepted this adjustment (pp. 411-16a). While the majority found the bondholders' criticism of the Commission's computations "not without persuasiveness," (p. 415a) it considered these criticisms offset by what it considered to be conservative aspects of the Commission's choice of a delay of only one year.*

As the majority noted, what was involved was "a never-never land" involving hypothetical events that never happened and will never happen (p. 411a). Unfortunately, in analyzing this 'never-never land," and the valuation date which the Commission had "picked" (see 289 F. Supp. at 438-39, p. 355a), the majority acted as though that date had real significance—and so concerned itself with the question whether, after sustaining enormous losses for seven years in the public interest so that railroad service could be kept going, the New Haven could in fact have commenced liquidation in the calendar year 1967. That question is indeed "never-never" land. As Judge Weinfeld pointed out (pp. 435a-36a), liquidation was out of the question in 1967, as it had been for several years, because by 1967 (in fact, at least as early as November, 1964) the New Haven was

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* The majority felt that this offset factors such as the following: (i) that only first year sales would be delayed, thus reducing the discount from $7.9 million to $4.1 million; and (ii) that preservation costs would be reduced because much of the equipment would be repossessed. The majority apparently failed to take into account other criticisms advanced by the bondholders, such as the following: (i) there was no competent evidence as to what the preservation costs would be; (ii) a substantial part of the "preservation costs" and taxes were operating costs which the New Haven had already incurred and thus were being duplicated by the Commission's computation; and (iii) while the Commission deducted $2.5 million for real estate taxes, it failed to credit the New Haven with an added $1 million of rental income (NHI-58, p. 14).

committed to inclusion in Penn Central,* and any effort toward liquidation would have been promptly rebuffed on that ground. In fact, the Commission in April 1966 rejected the New Haven Trustees' petition to abandon long-haul passenger trains in view of its decision that the New Haven would be included in Penn Central (327 I.C.C. 151, 219, 224, 523-27). Any effort to obtain Commission approval of abandonment after that date was plainly foredoomed.**

There is, we submit, nothing in the Commission's Report or in the majority opinion which suggests that, except for inclusion, the New Haven would not have obtained authority to abandon and commence liquidation long before December 31, 1966. The fact is, as the opinion of the Reorganization Court makes clear, that liquidation was an unavoidable step for the New Haven early in the reorganization, except that the hope of inclusion was thought to justify continuation in the public interest (pp. 283-85a).***

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* The New Haven Trustees had petitioned for inclusion in 1962 and had reached agreement, on November 9, 1964, with Penn and Central on the price to be paid when inclusion took place (NHI-1, pp. 28-31).

** The majority's suggestion that the bondholders in some sense waived any objection to abandonment before the end of 1967 also disregards the fact that the primary responsibility for managing the New Haven rested with the New Haven Trustees; they were at all times greatly, if not primarily, concerned with the public interest, and at least after November, 1964, were committed to the sale of the New Haven to Penn Central.

*** The majority also errs in asserting that the Bondholders had been contending before the Commission that NH could survive as a freight-only railroad. Appellant did offer expert testimony, responding to a contrary study of the New Haven Trustees, showing that a reconstructed New Haven, providing only freight service, would have had modest net operating income in 1964 and 1965, but the witness was careful to note that he was not attempting to project income for a period beyond 1965. This evidence was intro-

Thus, even on a factual basis, the majority's assumption that abandonment would not be feasible, absent inclusion, before at least the beginning of 1968, is inaccurate. Except for inclusion, that step would have been inevitable long before 1966.

Moreover, the Court incorrectly accepted the Commission's conclusion that delay for abandonment would have taken as long as one full year. This conclusion is not supported by substantial evidence. The primary reason for an abandonment delay is to allow the states, communities, and other interested parties an opportunity to present their plans for a takeover of the railroad. But in this instance, as the Reorganization Court observed, such persons had had 7½ years to present such plans and took no advantage of the opportunity (p. 283-84a).

Further, there is no competent evidence to support the Commission's conclusion that an abandonment delay of one year would have cost the New Haven $15,386,000. The Commission's figure rests upon the assumption that if the commencement of liquidation were to be postponed for a year, the only development during this time would be an erosion of the estate. What the Commission overlooked was that the assets, predominantly land, must then be revalued to December 31, 1967, and such revaluation, as both the Commission and the Three Judge Court previously noted (331 I.C.C. 698, 289 F. Supp. at 438-39, pp. 56a, 355a), was likely to be upwards. Moreover, the Commission ignored the

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duced solely on the issue of the fair price to be paid for the New Haven, in support of the Bondholders' contention that the subsidies for passenger service being paid by the states were too low, and in an effort to support the Bondholders' position that they were entitled to "going concern" value in addition to liquidation value, in view of suggestions in *Kimball Laundry Co.* v. *United States*, 338 U.S. 1 (1949) and *Matter of City of New York* [*Fifth Avenue Coach Lines*], 18 N.Y.2d 212 (1966) that potential profitability was a requisite to such an award.

following factors: (i) non-operating property could be sold immediately; (ii) sales contracts could be executed on a contingent basis; (iii) only sales scheduled for the first year would be delayed; and (iv) preservation costs would be less than estimated and offset by income, such as rental income, which the Commission disregarded. The effect of these factors is to substantially reduce, if not eliminate, the $15,386,000 estimate for abandonment delay cost.

The Three Judge Court conceded that several of the bondholders' arguments were "not without persuasiveness," (p. 415a) but nevertheless concluded that they are "offset" by the Commission's failure to deduct a further year's depreciation of $3,000,000 and to fix the delay in abandonment at two years rather than at one year.* The first suggested "offset" is insufficient. The effect of the points raised by the bondholders is far more than $3 million—annual rental income alone is $1 million; if only first year sales are affected by the delay, the reduction in the "discount" is in the order of $4 million; the Commission's errors in computing "preservation costs" are of a similar magnitude.

The second possible "offset" suggested, namely, the Commission's failure to assume that liquidation might be delayed until February 1, 1969 instead of January 1, 1968, is but a more extreme illustration of the confusion of hypothetical and real dates that is discussed above.

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* We argued below that the Commission's figure of $3 million for alleged 1966 depreciation is a *post facto* rationalization which is unsupported by the evidence. We make that same contention here.

B. The majority attempted to sustain the Commission's "bulk sale" discount on the basis of an analysis which the Commission did not make and which is not supported by the record.

The Commission further "adjusted" the liquidation value of the New Haven by an additional reduction of $6.695 million based upon its purported power to limit "the right to break up the railroad" (334 I.C.C. at 60, p. 147a). It argued that since it had the power to compel a sale in bulk to one who would undertake to operate the railroad, this implied the power to reduce the price below net liquidation value (334 I.C.C. at 60, p. 147a). The Three Judge Court rejected this analysis, saying

> ". . . we would suppose that the constitutional right to abandon operations implies a right to break up the railroad and sell the parcels for their highest and best prices." (p. 417a).

In fact, the Commission's argument was contrary to its consistent disposition of abandonment cases.* In those cases, while it required the seller to sell property in one piece to a buyer willing to operate the road, it was careful to note that the obligation was conditional upon the seller obtaining a price at least equal to "scrap value."

After rejecting the Commission's rationale, however, the majority of the Three Judge Court proceeded to construct a new theory on which it nevertheless sustained the Commission's adjustment. Judge Weinfeld described the majority's approach in these terms:

> "they purport to find justification for its acceptance by culling other statements from the Commission's report and deducing therefrom what the Commission really intended, to wit, a 'discount as a proper measure of

* See cases cited in the footnote to p. 16 *supra*.

risks not taken into account by the appraisals and the discount to present value.'" (p. 439a)*

As Judge Weinfeld noted, the theory of the majority of the Three Judge Court is altogether different from the one actually relied on by the Commission**; and moreover, it is contrary to the evidence.

Mr. Robert E. Simon, the witness who propounded the bulk sale discount theory, admitted that he had never seen any of the valuation study exhibits or read any of the testimony of the valuation or appraisal witnesses (Tr. 29823-34, 29855, 29858-60, 29878), many of whom were Penn Central's own witnesses (*e.g.*, Messrs. Gasparini, Hull and White). Thus, he could not have been in a position to determine what risks, if any, the appraisers had "not taken into account" (Majority opinion, p. 417a). The liquidation value studies already reflected substantial reductions to take into account expenses of sale and risks of sale. For example, the value of the property was discounted at the rate of 6% to compensate for the risks of delay, was decreased by $8 million as an allowance for distress sales at below market value, and further reduced by over $30 million to cover the cost of an elaborate corporate structure to handle demolition and sale and such direct costs of sale as brokerage fees and promotional expenses (NHI-42, pp. 38, 45; NHI-58, pp. 14, App. A).

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* The majority discerned this "risk theory" in the following remarks of the Commission: "The bulk sale discount merely reflects a market appraisal of the risks that the estate avoids, and that the bulk buyer assumes" (334 I.C.C. at 61, p. 148a); and a statement that the discount "fully recognizes, without conceding, NH's right to abandon and liquidate the estate." (334 I.C.C. at 63, p. 150a). The majority conceded that these remarks were "not pellucid" (p. 417a).

** The majority's approach, we submit, is indistinguishable from the course of conduct this Court condemned in *SEC* v. *Chenery Corp.*, 318 U.S. 80, 94 (1943).

The witness was admittedly unfamiliar with this evidence. What the witness did was to describe the process which he, as a purchaser of land in bulk with the intention to resell the land, would use to determine what he would pay. This process involved an appraisal of his carrying charges for borrowed money and a generous allowance (of 15% on his own investment) for his profit as an entrepreneur. This was the approach which the Commission adopted with certain modifications. It postulates a middleman, who buys in bulk for resale to retail users of land. While such a method of disposal is one of the possible courses a prudent management would investigate,* and presumably reject as too low in this case, it is not one which can be compelled by law.** Moreover, the Reorganization Court has held that it is not a method of disposal which it could approve under Section 77(b)(5) of the Bankruptcy Act. (Reorganization Court Opinion, pp. 292-93a.)

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* Other possible courses would seem more attractive, such as the parcel-by-parcel sales which the original valuation studies of the New Haven Trustees and Penn Central envisioned, the sale of large segments of the railroad on the basis of the probable interest of likely customers, including other railroads as well as real estate investors, operators and developers.

** The Commission obviously failed to note the basic distinction between its power to compel a sale "in bulk" at not less than scrap value to one who will continue railroad operations, and the sale in bulk to an entrepreneur who intends to dispose of the property piecemeal.

2. *The decision of the Three Judge Court errs in several substantial respects which bear importantly on the application of Section 5 of the Interstate Commerce Act and unlawfully deprive the New Haven of its property.*

A. The Three Judge Court's decision, while it recognizes that the New Haven's right to fully-paid access to and use of Grand Central Terminal may be a valuable asset, in fact accords this asset no value in determining the liquidation value of the New Haven.

The reviewing courts and the Commission have all agreed in holding that the New Haven, as Penn Central's partner in the development of the Grand Central Terminal Properties, is entitled to 50% of the "excess income" from all of those properties, *i.e.*, income in excess of that used to defray terminal expenses (pp. 117a ,118a, 253a, 295a, 418a, 419a). But neither the Commission nor the Courts have given any recognition, in terms of valuation, to the New Haven's admitted right to have approximately $5.6 million per year of Terminal Income (in addition to the so-called "excess income") used to defray the New Haven's portion of the expenses of the Terminal.*

As a result, since January 1, 1969, Penn Central's New Haven Division trains (*i.e.*, the former New Haven trains) have used the Terminal at the expense of the New Haven because the allocated cost of those trains, $5.6 million, was deducted before the amount of "excess income" to be capitalized in determining the sale price was computed. Penn Central retains all revenues from the trains.**

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* The annual expenses of the Terminal amounted to about $13.6 million annually in 1964-66. These expenses include primarily the handling of trains, freight and passengers in the Terminal and the cost of owning and operating Grand Central Terminal itself. The New Haven's share of these expenses—and of the income used to defray those expenses—based on its historic car-use ratio of about 41%, is $5.6 million per year.

** Since January 1, 1969, Penn Central has, of course, also received 100% of the "excess income" as well.

The Three Judge Court concluded, in its opinion of July 10, 1968, that this right to fully-paid access was without real value. The Reorganization Court, however, in its opinion dated August 13, 1968, concluded that the right represented "a valuable interest" which Penn Central had acquired (289 F. Supp. at 463, p. 253a) and directed the Commission to "make findings" as to what value, if any, attached to that right.

In its Fourth Supplemental Report, the Commission stated, "In liquidation the right to free use of the terminal would have no value to NH unless there was a buyer willing to pay for the use" (334 I.C.C. at 32, p. 119a). The Commission then concluded that the only potential buyer was the State of New York and that the right was valueless in those circumstances because the bargaining power of the State was so great that it would not "need to bid for free use of the terminal" (334 I.C.C. at 32, p. 119a).*

The Commission's conclusion and reasoning were accepted by the Three Judge Court in its decision of June 18, 1969. The Court recognized that if someone could be found to take over the New Haven's operations into Grand Central Terminal, then the right to fully-paid access would be a saleable right. But the Court concluded that the State was the only potential buyer, and the State would not be likely to pay for the right of access (p. 314a).**

It seems plain that both the Commission and the Three Judge Court agree that the right of fully-paid access to the Terminal is a valuable right if a buyer can be found.

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* Apparently, Penn Central has in fact reached agreement with New York and Connecticut. See the footnote at p. 28 *infra*.

** The Reorganization Court, in its Memorandum dated July 28, 1969, noted that its decision to accept the Commission's conclusion was not free from doubt and stated that if the right of fully-paid access were fully recognized it would have a potential value of $70 million (p. 314a).

And it is clear that there are at least two buyers for the New Haven's right—New York State and Penn Central itself, which is committed and compelled to acquire the property by reason of its own Agreement and Condition 8 of the Commission's order approving the Penn Central merger (p. 6, *supra*), which Penn Central accepted by merging. For both Penn Central and the State of New York, the New Haven's right to operate into the Terminal and to have Terminal income used to defray its expenses, has value.

By acquiring the New Haven's interest, Penn Central has acquired full and clear title to property which is worth at least $227 million (NHI-1, App. p. 3), and the undivided use of at least $18.4 million per year of income (334 I.C.C. at 39, p. 126a).

As the owner of this property, Penn Central is now (and was known at the time of the hearings to be) negotiating with Connecticut and New York to arrange for a New York State-Connecticut authority to take over the New Haven division commuter operations into Grand Central Terminal with Federal aid.* Whatever form that arrangement may finally take, Penn Central will have obtained some consideration for the use of the Terminal, which it now owns free and clear of the New Haven's rights. *Prima facie,* as the Commission recognized (334 I.C.C. at 32, p. 119a), the result of such an arrangement would be that the commuter authority would pay the "net cost of operating" the New

* In fact, since the record in this case was closed, it has been announced in the press that a joint instrumentality of New York and Connecticut has agreed to acquire the New Haven commuter service from Penn Central. We understand that as part of this agreement, the Commuter Authority will lease from Penn Central the track between Woodlawn, N.Y. and the Terminal and partial use of the Terminal itself under terms whereby it will pay $2.9 million per year. New York Times, November 26, 1969, pp. 1, 32.

Haven division trains into and out of the Terminal. Based on the record, that cost at present must be taken as substantially equal to $5.6 million per year.* Penn Central has acquired from the New Haven the New Haven's right to have $5.6 million of income, arising from the partnership enterprise, expended for its benefit to defray expenses which the New Haven otherwise would have had to meet by other means. The value of that right, we submit, is the capitalized value of an annual income of $5.6 million, or about $70 million using the Commission's capitalization rate for Grand Central Terminal "excess income" of 8%.

This conclusion, we submit, is not changed if, as a result of bargaining, the amount paid by the States is less than $5.6 million or even if Penn Central elects to bargain away this interest in order to get other advantages. What Penn Central chooses to do with the income-flow it has acquired is beside the point.**

B. The Three Judge Court's attempt *sua sponte* to remedy the Commission's gross overvaluation of Penn Central common stock by means of an "underwriting" fails to cure the overvaluation and thus leaves unremedied the substantial imbalance between the value of the assets sold and the value of the consideration received.

As part of the consideration for the assets it sold to Penn Central, the New Haven, on December 31, 1968, received 950,116 shares of Penn Central common stock. The

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* Depending upon the nature of the transaction, it may be necessary to reduce this figure by the allocated cost of long-haul New Haven long-haul passenger service, if Penn Central continues to be responsible for that service.

** We do not believe that this Court need determine the dollar value of the New Haven's right or even necessarily prescribe a method of valuation. In our view, the proper role of this Court is to disapprove the conclusion of the Commission and the Three Judge Court that the right need not be assigned any value at all.

Commission valued this stock at $87.50 per share, a total of approximately $83.1 million or roughly 60% of the total value if assigned to the consideration paid (331 I.C.C. at 688-90, 692; 334 I.C.C. at 68; pp. 46-48a, 50a, 155a). At the end of 1966, the valuation date applied to the New Haven assets, the average price on the New York Stock Exchange was 52⅜. On December 31, 1968, the date of the inclusion, the stock closed at 63⅜. The market price of the stock has steadily declined; on December 3, 1969, it closed at 29⅛.

Both courts rejected the $87.50 valuation as inflated (pp. 299-300a, 429-30a). In its decision of May 28, 1969, the Reorganization Court attempted to meet the objections of the bondholders to the $87.50 price by providing, on its own motion, for an "underwriting" formula whereby Penn Central must, in essence, pay the difference between the average market price of the shares in the 30-day period prior to February 1, 1978 and $87.50 per share, unless Penn Central stock reaches and maintains a price of $87.50 for five consecutive days in the approximate nine-year period intervening (pp. 300-01a). The Three Judge Court essentially followed the Reorganization Court.* The Commission has apparently accepted this modification in principle (334 I.C.C. at 532, p. 226a).

While the "underwriting" formula is a substantial improvement in the terms of inclusion, it nevertheless falls far short of what the New Haven is entitled to. In the first place, since the obligation is neither secured nor entitled to any priority over general creditors, the "underwriting" formula fails to accord the New Haven any protection against the risk of insolvency or reorganization of Penn Central during the intervening nine years, during which the New Haven's right cannot be transferred. In the sec-

* Judge Weinfeld dissented on this point (pp. 441-42a).

ond place, the "underwriting" formula disregards the fact that a payment to be received nine years in the future is worth substantially less than a payment made today. Assuming a 6% discount rate,* the one generally used by the Commission, and using the market price (43-44½) for the stock at the time of the Three Judge Court's decision (August 5, 1969), the value of the stock portion of the consideration (including the "underwriting") which the New Haven has received is at least $17 million less than the $83.1 million value assigned to the stock by the Commission.**

Thus, even after taking the "underwriting" formula into account, the consideration paid by Penn Central is worth at least $17 million less than the adjusted net value assigned by the Commission to the New Haven assets. This result is wholly contrary to the constitutional and statutory standard of fairness and equity, namely, substantial equivalence between the value of the assets sold and the value of the consideration paid, which both the Commission and the Courts have found applicable here.

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* Of course, a discount rate higher than 6%, which may seem more appropriate in the present money market, would give a significantly lower present value; thus, at a 6% rate, $1 to be received in 9 years would be worth 58.1 cents; at an 8% rate it would be worth only 48.5 cents.

** At the time of the Three Judge Court's opinion (August 5, 1969), the market value of the stock was approximately $41.5 million, or about $41.6 million below the Commission's value of $83.1 million. The present worth of $41.6 million payable nine years hence, is only about $24.2 million. Thus, the value of the stock plus the present value of the "underwriting" was then only $65.8 million.

C. The Commission's decision to accept one appraisal of the New Haven's Harlem River and Oak Point Yards, and reject an appraisal $4.5 million higher, was unconstitutionally made on the basis of matters dehors the record and is not supported by substantial evidence.

The New Haven's Harlem River and Oak Point Yards are two large freight yards, totalling about 160 acres, which are located in the Southeast Bronx, along the main freight line of the New Haven and about a mile apart. Tracks running through the Oak Point Yard constitute the only rail link between Penn Central's Port Morris branch and the Hunts Point Market, a central market recently built by New York City, at a cost of well over $100 million, and still being expanded to handle the bulk of the perishable produce brought into New York City.

Four appraisals of these yeards were submitted in evidence during the first hearings. The bondholders' witness, Paul O'Keefe, appraised the yards at $32 million, assuming a residential use for the yards, and at $26 million, assuming an industrial use. Penn Central submitted an appraisal of $15.585 million, and the New Haven Reorganization Trustees submitted two appraisals—one of $22.65 million and another of $18.1 million—prepared by Mr. Arthur McCann, all of which assumed an industrial use. The Commission, in its Second Supplemental Report (331 I.C.C. at 668, p. 26a), accepted the $18.1 million appraisal, the second and lower of the two McCann appraisals. In its first opinion, the Three Judge Court disapproved the Commission's conclusion on this point, noting that it had inadequately explained why it chose the $18.1 million appraisal rather than the other McCann appraisal of $22.65 million, or the $26 million appraisal of Paul O'Keefe (289 F. Supp. at 434, p. 345a).

On remand, Mr. McCann testified that his two appraisals differed because in the higher one he assumed that there was "rail facilities" to the yards, and in the lower one he assumed no such "rail facilities" (Tr. 28848-49, 28854, 28862).* He confessed that in making his appraisals he was unaware that there was a physical connection between Penn Central's Port Morris branch and the Oak Point Yard (Tr. 28881; cf. R. 27, pp. 2-3). Both Penn Central's witnesses and the bondholders' witness testified that there would have to be rail service to Hunts Point (Tr. 29455, 29683-84, 29693-94). Since the only nearby rail connection to Hunts Point is Penn Central's Port Morris branch, via the Oak Point Yard and a short section of the New Haven main line, this service would have to be run through the Oak Point Yard.

In its Fourth Supplemental Report, the Commission adhered to its earlier position and again accepted the lower $18.1 million McCann appraisal, because it assumed that there would be no "rail service" to Hunts Point (334 I.C.C. at 42-43, pp. 129-30a), although this view contradicted the evidence of Penn Central's witnesses, as well as the bondholders' witness. The Commission concluded that Penn Central probably had no legal obligation to provide service (334 I.C.C. at 44-45, pp. 131-32a) and would choose not to do so, because, in its view, such service would not be economically attractive since it involves perishable produce. The Commission held that such traffic is unprofitable—and presumably always will be—not on the basis of any evidence in the record, but by the use of material it

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* Mr. McCann explained that, based on his experience with other industrial parcels in the Bronx, he had found that land with "rail service" sold at about 10% higher than land without "rail service" (see Tr. 28854).

had gathered from reports filed by other railroads for the year 1965, before Hunts Point was built and before the Commission had given several general rate increases (see 334 I.C.C. at 45-47, pp. 132-34a).

The majority of the Three Judge Court affirmed the Commission, apparently on the basis of its assumed "expertise". Both Judge Weinfeld, in dissent, and the Reorganization Court found to the contrary. Judge Weinfeld wrote:

> "[The Commission's] finding as to non-operation of the yards made with respect to Penn Central, any existing terminal carrier, a new terminal carrier or the City of New York does not appear to be based upon substantial evidence. It is difficult to agree that an important rail service to industrial users would be terminated and the line dismantled. Nothing in the record supports the Commission's assumption that the properties would be stripped of their trackage and electricity, both highly desirable industrial features, and the former alone commanding about a 10% premium in Bronx realty values. The Commission's finding of value of $18.1 million is without substantial evidential support, particularly in the light of the appraiser's testimony as to the incorrect basis of his lower valuation; at the minimum, the value is the higher of his appraisals, $22.650 million."* (pp. 442-43a)

The Reorganization Court wrote:

> "To assume that the State and City of New York would stand idly by and permit the life line to its huge and costly enterprise to be cut, just as it is in the midst

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* Judge Weinfeld no doubt had in mind the fact that the Commission had failed to explain why it rejected Mr. O'Keefe's $26 million appraisal.

of planning its necessary enlargement, because it was unwilling or unable effectively to bring pressures to bear or take steps on its own to preserve the connection with Penn Central is absurd, even if the I.C.C. continues its policy of forcing the railroads to handle perishable produce at a loss." (p. 297a)

In accepting the $18.1 million appraisal, the Commission made two major errors:

(1) it relied for its conclusion on material outside the record without permitting Appellant any opportunity to even learn of the existence of the material until its decision was published; and

(2) it made a finding which is unsupported by the evidence and in fact is contrary to the evidence.

D. The Commission's computation of the discount to present value of liquidation receipts, which the Reorganization Court rejected as erroneous and the Three Judge Court left for decision by this Court, is unsupported by substantial evidence.

During the hearings on remand, both Penn Central and the bondholders introduced evidence which established that the Commission's figure for the discount necessary to determine the present worth of the gross proceeds of liquidation (which were to be received over the six-year liquidation period) was too high. The bondholders' witness (Dr. Altman) showed that the figure was too high by approximately $2.5 million (R-39, p. 9); Penn Central's witness, Mr. Hull, found that it was too high by $600,000 (R-38, p. 10). Nevertheless, the Commission has refused to reconsider its computation, despite ample opportunity to do so.

In their decisions reviewing the Commission's Second Supplemental Report, the Three Judge Court and the Re-

organization Court directed the Commission on remand to reconsider the effect of "expenses of liquidation" in computing discounted future liquidation receipts. Pursuant to this direction, the Commission received evidence (namely, the Altman and Hull testimony) on the present worth of gross and net liquidation proceeds and of gross liquidation expenses. In spite of this full record, which showed that its figure for the discount of gross liquidation receipts was wrong, the Commission confined itself to adjusting liquidation value to take into account a discount of gross liquidation *expenses*. It concluded that the Court's direction on remand did not obligate it to reconsider its computation of the discount for gross liquidation *proceeds*, and the Commission chose not to do so. Consistent with this narrow view of its role, the Commission, in its Fifth Supplemental Report, again refused to fully reconsider its figure for gross liquidation proceeds although, because of the various changes in asset valuation, it had to adjust that discount downwards by $410,000.*

The two members of the Three Judge Court who signed the decree (Judge Weinfeld apparently did not participate) accepted the Commission's discount without passing on its merits, apparently on the ground that the analysis needed to make any different calculation was not before it except in the briefs on its decree,** but suggested that this "will be another matter for ultimate resolution by the Supreme Court" (p. 445a).

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* Among the results of the Commission's obduracy was the fact that in making this adjustment, it purported to "reduce" the discount on sales of passenger equipment although the figure it relied on took no discount for the proceeds of such sales (see p. 224a).

** In so holding, we believe, the majority was mistaken. The requisite evidence was already in the record; the briefs simply provided a different analytical approach from that used by Dr. Altman and Mr. Hull.

The Reorganization Court, after oral argument and extensive briefs, found that the Commission's computations were incorrect and adjusted the discount of net proceeds downwards by $2.4 million (p. 318a).

We submit that the record fully supports the Reorganization Court's decision, and establishes that the Commission was in error. Yet the Commission refused, in spite of clear agreement that its figures are wrong, to make a correction which fairness and justice plainly require.

E. The Three Judge Court's acceptance of the Commission's view that "going concern value" is an alternative method of valuation rather than an additional element of value in determining liquidation value misconceives and ignores the effect of applicable state law, and thus unlawfully deprives the New Haven of value to which it is entitled.

Although the evidence showed that the "going concern" value of the New Haven was $55 million and the Commission found in effect that it was $5.5 million (331 I.C.C. at 684-85; pp. 42-43a), the Commission treated "going concern value" as an alternative means of valuation to liquidation value, and therefore disregarded the reduced "going concern value" it found since this value was far less than liquidation value. Both courts affirmed the Commission on this point (289 F. Supp. at 435 and 454-55, pp. 239-40a, 347-49a). In so doing, we submit, both the Commission and the Courts misconceived the impact of the condemnation law of New York State and applied a measure of value which this Court should reexamine in the light of recent developments in condemnation law.

New York law is now well settled that where a public utility (regardless of its profitability) is taken by condemnation and is to be continued in operation by the purchaser, the seller is entitled, not simply to the scrap or liquidation

value of the assets sold, but to an additional value because it is a going concern. *Matter of City of New York (Fifth Avenue Coach Lines)*, 18 N.Y.2d 212 (1966); *Matter of Port Authority Trans Hudson Corp.* v. *Hudson Rapid Tubes Corp.*, 20 N.Y.2d 457 (1967), *cert. denied*, 390 U.S. 1002 (1968) (the "*PATH* case").

The facts presented here essentially parallel those in *PATH* and *Fifth Avenue Coach*, in that a unique public utility has been taken over in the public interest, and is intended to be continued in operation. Moreover, it would seem that in this case, there is a substantial probability that a large portion of the New Haven's New York-based assets will ultimately be sold to an instrumentality of New York and Connecticut.*

In these circumstances, we submit that, at least as to the New York-based assets of the New Haven, the Commission and the courts erred in failing to adopt the standard of valuation required by the condemnation law of New York, and should have awarded the substantial added compensation for "going concern" value which that State's law provides. We further submit that this case is an appropriate one for this Court to determine the proper role of "going concern" value under federally-based valuation law in situations where a public utility is to be continued in operation.**

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* Apparently, Penn Central has agreed to such an arrangement. See the footnote on p. 28 *supra*.

** *Cf. Kimball Laundry Co.* v. *United States*, 338 U.S. 1 (1949), which suggests that a rule similar to that of New York may be applicable to a taking under federal law.

F. Under the terms of the Commission's order approving the merger of Penn Central and of this Court's affirmance of the merger, Penn Central should be required to assume all of the New Haven's operating losses for the eleven months between the effective date of the Penn Central merger and the date of inclusion of New Haven operations.

The New Haven was kept in operation, as the Reorganization Court has observed (p. 285a), in spite of steadily mounting losses, in order to preserve it for inclusion in Penn Central and thereby serve the public interest by preserving its operations. We do not believe there is any serious question that Penn Central's agreement to acquire the New Haven weighed heavily in the finding that there was a public interest requisite to support the merger.

Had the New Haven been included in Penn Central at the time of the merger, rather than eleven months later, Penn Central would have assumed all losses after the merger. As Judge Weinfeld pointed out in his dissent, inclusion would have occurred at merger "[h]ad that which should have been done, been done . . ." (p. 378a). The only reasons inclusion did not then occur were that Penn Central would have found it inconvenient to do so and was reluctant to assume a conditional liability. The New Haven gained nothing from the delay but further dilution of a security already made meager by seven prior years of loss.

Shortly before the final oral argument in this Court on the merits of the merger, the Commission, responding to a suggestion of the Reorganization Court, included in its Second Supplemental Report so-called "interim" provisions (331 I.C.C. at 699-721, pp. 57-78a) to keep the New Haven going pending inclusion by providing cash and by meeting the objections of the Bondholders to the imposition of further losses. The adequacy of these provisions was then argued in this Court at some length.

While the Commission projected that the "loss-sharing" formula it developed as a major aspect of these "interim" provisions would cover 100% of the operating losses of the New Haven during the first year after the merger (331 I.C.C. at 718-19, pp. 76-77a), the Commission later conceded that it fell far short of that percentage (334 I.C.C. at 73-74, pp. 160-161a).*

In these circumstances, we submit, this Court should consider whether it is consistent with the standard of fairness and equity of Section 5 of the Interstate Commerce Act or with the intent of this Court in permitting the Penn Central merger to go forward without requiring simultaneous inclusion, to impose a major portion of the interim losses on the New Haven. Such a result, we submit is neither fair nor equitable.

G. Other substantial errors which should be reviewed.

For brevity, we merely enumerate other aspects of the Three Judge Court's decision which, we submit, substantially deprived the New Haven of the fair value of the property it sold:

1. The Court affirmed the Commission in substantially undervaluing or treating as valueless the New

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* The Commission projected operating losses under its formula at $8.2 million for the year 1968, $2.7 million more than the $5.5 million "ceiling" it imposed under the formula, and awarded the New Haven a lump sum of $5 million for the eleven months between merger and inclusion (334 I.C.C. at 73-74, p. 160a). On these computations, the New Haven bore approximately $2.5 million of losses, out of total losses, computed under the formula, of approximately $7.5 million for the eleven month period. In the Bondholders' view, the actual losses of the New Haven during 1968 were in the order of $15-17 million, and thus the New Haven bore $10-12 million of interim losses.

Haven's investments in several other companies, including New York Connecting Railroad Company and Railway Express Agency, Inc.

2. The Court approved the reduction of the liquidation value of the New Haven's road property by $3 million for alleged "depreciation" during 1966, although this adjustment was unsupported by the evidence and contradicted by Commission counsel's own previous analysis.

CONCLUSION

For the reasons stated, the questions presented are so substantial as to require plenary consideration, with briefs on the merits and oral argument, for their resolution.

Respectfully submitted,

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